Testimony of
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U.S. House of Representatives

Hearing on
The Need for Comprehensive Tax Reform to Help American Companies Compete in the Global Market and Create Jobs for American Workers

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Chairman Camp, Ranking Member Levin, and members of the Committee on Ways and Means, it is a privilege to be here to testify on the need for pro-growth tax reform. I am here as the chief financial officer of an established American manufacturing firm that does business, and aims to succeed, around the world.

BACKGROUND ON UTC

United Technologies Corporation (UTC) is an American company with headquarters in Hartford, Connecticut. We provide high-technology products and services to the global aerospace and building systems industries through our diverse business units:

- Carrier heating, air-conditioning and refrigeration solutions;
- Hamilton Sundstrand aerospace and industrial systems;
- Otis elevators and escalators;
- Pratt & Whitney jet engines;
- Sikorsky helicopters;
- UTC Fire & Security systems and services; and
- UTC Power fuel cells.

Our company identity stems from our history of having been built by inventors. Many of our business units are named after pioneers whose innovations transformed the way people live and work. Gifted inventors like

Willis Carrier, Elisha Graves Otis, and Igor Sikorsky laid the foundation of United Technologies and left a legacy of innovation that our 205,000 employees continue to this day.

In addition to being an iconic American company, UTC is truly a worldwide organization. About 40% of our sales are earned in the United States, and the remaining 60% in other countries. The location of our workforce roughly tracks this split of sales. UTC has over 4,000 facilities across 71 countries. The company conducts business in virtually every country in the world as well as in all 50 states.

With this scale comes the ability to make positive contributions in the marketplace and communities where we invest. Last year, UTC spent $3.6 billion on company and customer funded research and development, the lion's share in the U.S. We exported over $7 billion in products and services. We match our employees' charitable contributions through various giving programs to many worthy causes. Through our Employee Scholar program, UTC has invested nearly $1 billion to fund more than 30,000 educational degrees with no time commitment or financial payback required.

TAX CHALLENGES FOR U.S. COMPANIES IN A COMPETITIVE WORLD

Worldwide Taxation, High Statutory Rate

UTC is a publicly traded, NYSE listed, Fortune 50 enterprise. We are organized and pay taxes as a corporation. Because we are an American company, we are subject to tax on our worldwide income, no matter where it is earned, at the federal corporate tax rate of 35%. Combined with state income taxes, the U.S. statutory income rate imposed on corporations hovers at or near the highest among all developed economies. If the rate-lowering trend of our trading partners continues, the U.S. may soon, to its peril, be "number one."

These facts present a competitive difficulty that is becoming more and more typical for U.S.-based firms doing business around the world. That is, our non-U.S. competitors generally only pay taxes in the country in which their income was earned. They pay little or no taxes in their home country on overseas earnings.

The U.S. system for taxing its corporate citizens on their global income, even with the deferral feature, is an outdated remnant that inhibits our ability to compete globally and discourages reinvestment of overseas earnings in the United States. In fact, our system actually hinders success. It was designed when the U.S. was the dominant economy, and before globalization became an unmistakable market reality.

Policy Uncertainty

In today's global economy, capital is mobile. Competition is everywhere, and so are the growth markets where we need to compete in order to succeed. In such an environment, the focus of the tax code should be on the most efficient way to generate the revenue necessary for the government while allowing American companies to contend for business in markets around the world. Unfortunately, U.S. tax policy uncertainty acts more as an impediment to success than an enabler of it.

The R&D credit is a perfect example. In 2010, for the fourteenth time, this credit was allowed to expire. It was not re-enacted until December 17, when it was retroactively reinstated. These developments created a situation in which decisions on our most important investments, those that create intellectual property and innovation, had to be made without regard to the potential tax credit. Not only does this approach to tax policy undermine business decisions, it undermines prospects for American workers by inadvertently encouraging the migration of engineering and development activities to countries with more predictable, more favorable tax treatment.

Another example of uncertainty that is directly related to international competitiveness is the tax code provision known as "CFC look-through." This provision facilitates the kind of modern organizational structures that UTC and other companies use in their worldwide operations, managing debt and other financial activities on a regional basis. From a corporate treasury perspective, it allows capital to be put to its most efficient use. Active earnings under this provision can cross a country border within the regions where we operate, such as in Western Europe or Asia, without triggering a U.S. tax consequence.

Unfortunately, the CFC look-through provision is also subject to the annual extender legislation process. The uncertainty created by legal lapses and short-term extensions is a hindrance to growth, efficiency, and sound planning. In the business world, a company that delivered on its promises more than eleven months late or kept its customers wondering what it could and could not do would feel marketplace consequences. Similarly, taxpayers need to know what they can and cannot count on in the tax law.

Tax Complexity

The complexity of our tax system is another costly hindrance to sound business planning. Because of its size, UTC is under continuous IRS audit. At any given time there are ten to twelve IRS agents on site at our headquarters, full time, year round. Our federal tax return is almost 19,000 pages. And that's just federal income taxes.

Complying with the tax laws is UTC's obligation as a corporate citizen. Our core ethical values are paramount, and compliance with laws and regulations is non-negotiable. But doing so comes at a price in terms of the time and productive resources that could otherwise be more efficiently employed. Simplifying the tax code where possible would drive down costs and make meeting our obligations less cumbersome. The U.S. economy, the government, and taxpayers would all benefit.

Tax Policy Impediments to Growth

The anti-competitive tax burdens which the United States places on its own companies become apparent when those companies attempt to grow through acquisition.

I was recently asked on an analyst call about a rumor that UTC would acquire a company with Swiss headquarters. It was not a tax question, but it inadvertently raised serious tax policy issues. According to the most recent OECD listing, Switzerland's income tax rate is 18 percentage points lower than that of the U.S. Furthermore, Switzerland only taxes income earned within its borders; earnings brought home from other jurisdictions are not taxed. By contrast, profits brought home by a U.S. corporation from its worldwide operations are subject to a top-up tax at 35%.

The answer to the analyst's question was obvious: as an American firm, UTC would be disadvantaged in trying to buy the Swiss company. The favorable tax characteristics of the target company would be lost if it suddenly became a subsidiary of a U.S. parent. In short, the tax drag would kill the deal. A more likely result would be that a foreign buyer would win the opportunity to acquire the Swiss company. They, not the American firm, would reap the benefits that could include increased market share, access to a key supplier, greater cost synergies, or efficiency gains.

This example is representative of the challenges American companies face regularly. At UTC, our business units grow by developing game-changing technologies and providing superior value to customers, but they also look for opportunities to grow through acquisitions. Strategic acquisitions create opportunities for all of our stakeholders: employees, suppliers, communities, and shareowners. Yet in pursuing these opportunities, American companies bear a tax cost that their foreign competitors do not.

For American worldwide companies, the sad result of these structural defects in the tax system, over the long run, is that those who cannot win opportunities for growth abroad will inevitably shrink their capacity to export, see fewer headquarters and support positions at home, reduce their footprint in the marketplace, and curtail business for their local supply networks, which are often small and medium-sized companies. What is needed is a tax code that puts the U.S. on an equal footing with the competition.

USING SOUND PRINCIPLES TO FIND TAX REFORM SOLUTIONS

Many tax experts, academics, practitioners, and taxpayers have testified and provided input into the tax reform process, and many more will do so as these issues continue to be examined. As Congress considers changes to the tax system, my perspective as a finance officer leads me to offer the following recommendations:

1) Remember economic fundamentals.
2) Benchmark.
3) Take a measured approach.

In business, decisions are made after considering many factors, but must rest on economic fundamentals. We cannot ignore economics if we are going to plan for successful results over the long term. Similarly, policy makers should know that the worldwide imposition of tax (even with deferral), the costs of complexity and uncertainty, and the distortive impact of narrowly focused policy choices have consequences that are not conducive to job creation. It follows that fixing these problems will make American companies more competitive.

The second recommendation, benchmarking, goes hand-in-hand with the first. When UTC's businesses are trying to solve a problem or improve a process, we benchmark against our peers and those companies known for excellence. We look for best practices, then we try to emulate them with adjustments for our own facts, culture, values, and circumstances. A benchmarking exercise comparing the United States with other countries on how we tax businesses would reveal the unmistakable fact of the high U.S. income tax rate, whether statutory rates or effective rates are examined. It would also show how uncompetitive the U.S. is with its worldwide system and insistence on reaching around the globe to tax its home companies.

Clearly, a better system can be designed. It doesn't have to be perfect. There are various ways a territorial system could be implemented that would vastly improve American efficiency and reduce the current prohibitive cost on bringing home income earned abroad. But it should be a system that is competitive with our trading partners.

Disallowing legitimate expenses incurred here would be a job-killing mistake, replacing one set of special burdens on American companies for another. Likewise, keeping the current system, but repealing deferral, would make the U.S. even more of an outlier than it is today. If Congress follows sound benchmarking practices, tax reform will produce a growth-oriented tax system that draws wisdom from other jurisdictions but is still uniquely American.

Finally, I would urge the Congress to take a measured and balanced approach in legislating on tax reform. An open process such as the hearing today, allowing a comment period when drafts are released, and continuing bipartisan discussions will help create a final product with the potential to attract broad support. In this effort, the perfect should not be the enemy of the good, and the good will broadly benefit the American economy.

UTC is aligned with the broader business community when we say we don’t want tax reform to overburden the U.S. Treasury. We’re committed to a fiscally responsible approach. We want rules in place to prevent tax evasion. We know we have to give up some current benefits in order for tax reform to succeed. We hope that political name-calling can be filtered out. American companies should not be punished for serving global customers or succeeding in multiple markets.

By adopting a businesslike problem-solving approach, policymakers can design a tax system that balances the government’s obligations with the goals of providing greater tax certainty, reducing complexity, and improving American competitiveness.

CONCLUSION

It is time to modernize the U.S. tax system. Reforms should be agnostic, avoid picking winners and losers, and acknowledge the reality of globalization without punishing the business community. Having competitive tax rates and a competitive territorial system are worthy goals that ultimately increase confidence, create certainty, and ensure good jobs for America. These reforms will enable both old and new companies with American headquarters to succeed today and in the future, sharing their products, services, talents and technologies with the world.

Thank you.